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EDITORIAL DEPARTMENT NOTE

Depreciation, inventories, and standards—articles on these three subjects in this issue of the *Bulletin* are suggestive of three areas in which the industrial accountant will be busily engaged in the months immediately ahead. Professor Norton presents a challenging viewpoint on the spreading of the cost of assets over time through depreciation charges; Mr. Atchison outlines a procedure for the taking of physical inventories which will be of interest at this time when companies are reviewing procedure for taking their first postwar inventories; and Mr. McNeill points to some limitations of standard cost accounting and suggests remedies.

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Articles published in the *Bulletin* present many different viewpoints. In publishing them the Association is not sponsoring the view expressed, but is endeavoring to provide for its members material which will be helpful and stimulating. Constructive comments are welcomed and will be published in the Forum Section of the *Bulletin*.

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DECEMBER 1, 1945

AN ENGINEERING VIEWPOINT ON DEPRECIATION ACCOUNTING

By Paul T. Norton, Jr., Professor of Industrial Engineering, Virginia Polytechnic Institute, Blacksburg, Va.

IT IS more than twenty-five years since I first became interested in the depreciation problem. The Ohio Manufacturing Company with which I was then connected had a dispute with the Bureau of Internal Revenue concerning the amortization of war facilities. Many of us will be having the same problem within the next few months. After having been dormant for many years, my interest in depreciation again became very active when T.D. 4422 was issued early in 1934. At that time I was looking for industrial problems that were important enough in the minds of Virginia manufacturers to make them willing to listen to me when I attempted to show them how to diagnose and solve these problems. Beginning in 1934 I preached depreciation at every opportunity, had more than a score of articles on the subject published in engineering and trade papers, spoke at many meetings, and served on a number of depreciation committees. These activities have convinced me that engineers, accountants, and business men are faced continuously with the necessity of solving important and difficult problems in the field of depreciation.

Life Expectancy of Fixed Assets

Ten years ago it seemed to me that the expected lives used by the Bureau of Internal Revenue in setting depreciation rates under T.D. 4422 were in most cases too long and that the depreciation rates so set were therefore too low. I should almost certainly not have condemned the use of straight-line depreciation with rates based on actual service lives. At present I can only say that while I am just as sure as I ever was that the depreciation rates set by the Bureau of Internal Revenue are much lower than they should be, my reasons for thinking so are very different.

The truth is that the Bureau is perfectly consistent with the facts shown by their actuarial studies of average service lives of equipment. In my opinion we can never hope to persuade the Bureau that its rates are too low unless we rid ourselves of the

idea so prevalent among engineers, accountants, and business men that there is something inherently correct in straight-line depreciation with rates based on actual service lives.

Allocating Depreciation to Years of Life

It seems to me that what all of us, taxpayers and Bureau alike, must do is to recognize the fact that the depreciation accounting problem is fundamentally indeterminate. The reason for this indeterminateness is not generally understood. It is not primarily because of the difficulty in estimating the prospective life of assets. The basic trouble is that, given a life, first cost, and salvage value, there is no one right method for allocating the difference between the first cost and salvage value among years of life. In the literature of depreciation accounting many different criteria are advocated for judging the various possible ways of making this allocation. These criteria which are recommended for judging the relative merits of various depreciation methods can be applied in any set of circumstances to methods such as straight line, sinking fund, fixed percentage of diminishing balance, production units, and others. Nevertheless, the fact remains that it is impossible to state that one method is right and the others wrong; one may merely say that they correspond well or badly to various criteria which were established as a basis for their comparison and the respective merits of which are debatable.

Neither accountants, engineers, nor industrial managers seem to be fully aware of all the changes in the actual practices in depreciation accounting which have taken place since 1934, particularly in the manufacturing industries. Before T.D. 4422, although lip service was paid to straight-line depreciation accounting, the lives used in setting depreciation rates were generally much shorter than actual service lives. For example, a common rate on manufacturing equipment was 10 per cent, even though it was often evident that average service lives were much longer than 10 years. This had the effect of concentrating the depreciation write-off in the early years of life. In my opinion, this was, in many respects, really a very desirable state of affairs, as it charged off the investment in those years when the asset was most able to earn this investment.

Policy of Bureau of Internal Revenue

The present practice of the Bureau of Internal Revenue aims at true straight-line depreciation accounting, based on the best possible estimate of the full service life to the taxpayer. The Bureau will permit other methods, but their approval seems to depend on how closely the results conform to the straight-line method, which apparently means that a taxpayer dissatisfied with the straight-line method, using rates approved by the Bureau, can hardly hope to be better satisfied by any other method that the Bureau will approve. The fundamental difficulty seems to be that the so-called straight-line method used before 1934 was in most cases not at all what the advocates of straight-line depreciation really thought it was, and when the Bureau followed the issuance of T.D. 4422 by making rate reductions, the complaints of aggrieved taxpayers were directed at the point where the Bureau's position was the strongest, namely, the estimated service lives. As a matter of fact it is difficult to disprove the life estimates of the Bureau. Unfortunately in many cases the taxpayer does not even seem to be getting those rates which would be justified upon the basis of full estimated service lives. For example, consider an asset which when T.D. 4422 was issued was 5 years old and had been depreciated at the rate of 10 per cent per year. The Bureau then decided that the full estimated service life should be 15 years instead of 10 years, and proceeded to reduce the rate for the remaining 10 years of estimated life to 5 per cent per year. It is evident that even if the Bureau were correct in the life estimate, a 15-year life should result in a rate of 6⅔ per cent per year. The only reason for the 5 per cent rate is to average down the supposedly too high rate which had been used for the first five years of life.

In the average manufacturing company it is very unusual to make actuarial life studies, and the Bureau never bothers to change current depreciation rates upward, although they often go back and in effect reduce the future opportunities for charging depreciation by claiming that the depreciation charged in past years was less than that "allowable." Is it not reasonable to assume that as time goes on, the 5 per cent rate being charged on the asset of this example may become established in the minds

of the accountants of this company as the proper rate on this sort of asset? If other similar new assets are later purchased, is it not likely that the rate on them will be set as 5 per cent, instead of the 6⅔ per cent that the Bureau would allow based on full estimated service life, or the 10 per cent which the true economic facts of life might well justify?

From all indications the Bureau of Internal Revenue people remain serenely convinced that their policy of setting depreciation rates on the basis of straight-line depreciation with full estimated service life is a perfectly proper and scientifically correct method. I must say that if I were they, the arguments generally used against their policy would not be very convincing to me. What we need, in my opinion, is to get rid completely of the "sacred cow" of straight-line depreciation based on full service lives. If we can once do that we may find that government and taxpayer can get together on a basis that is mutually satisfactory and that can be justified as being as nearly correct from the standpoint of economics as anything so indeterminate can possibly be.

While the Bureau shows no signs of permitting higher rates than those based upon straight-line depreciation and full estimated service lives, many high government officials have been advocating high depreciation allowances in the early years of assets purchased in the immediate postwar period than would be permissible under present regulations of the Bureau. The purpose of this suggestion is, of course, to increase employment by giving the taxpayer a tax incentive to purchase assets which he would not otherwise purchase. All of us want maximum employment that would result from the largest reasonable amount of investment of private capital in depreciating assets, but I am sure that most people will agree with me that tax expedients which are economically unsound are not desirable. In fact, I suspect that in general "tax incentives" are undesirable, as a government which offers a "tax incentive" today is very apt to apply a "tax penalty" tomorrow. The truth is that in most cases anything that is a "tax incentive" for one taxpayer is at the same moment a "tax penalty" to other taxpayers.

Necessity for Rapid Depreciation

While I am not in favor of an unsound tax expedient for even such a good purpose as the increase in the rate of private capital investment, I am inclined to believe that in this particular case the liberalization of depreciation tax policy can be justified as sound economics resulting in increased private capital investment.

Even those manufacturers who act as though they believed in straight-line depreciation seem to sense the fact that the investment in an asset should be charged off through depreciation more rapidly in the early years of life. At least they are apt to act this way when considering the purchase of an asset. For example, a manufacturer is apt to have a policy requiring that a proposed asset will not be purchased unless it will "pay for itself in three years" or in some similar period much shorter than the estimated prospective service life. I shall attempt to explain why there is nothing inconsistent in such a policy, and why it seems to me that there is a sound economic reason for permitting higher depreciation allowances in the early years of all assets, not merely those purchased in the immediate postwar period.

A principal reason for higher depreciation rates in early years lies in the fact that it is often economical to continue to use assets long after they no longer are able to earn either a return of capital or a return on capital in competition with assets which might be purchased to replace them. Under such circumstances any investment in the present asset which has not been returned out of earnings will never be returned, and if this asset is considered alone, there will be a capital loss. Income taxes which previously have been paid on the apparent but unreal earnings of this asset will have been a capital levy under the guise of an income tax. It is probable that there are many cases of this sort, although it is difficult to locate them because it is seldom that the operating results of individual assets are segregated. The following example is admittedly an extreme case, but there is no doubt whatever that there are many unsuspected cases of this sort in which the owners of assets are severely penalized from the standpoint of federal taxes. Such owners may have attempted to protect themselves by insisting before

purchase that assets must pay for themselves in a comparatively short period, but it can be proved by simple arithmetic that with present high tax rates and the present depreciation policy of the Bureau, it is often impossible for the owner to recover the investment in an asset, no matter how profitable that asset may appear to be on the books.

An Illustrative Case Study

In this example the present asset is 10 years old, its second-hand value is $2,000, and it is estimated that this second-hand value will not decrease materially within the next few years. The asset had an original cost of $22,000, and straight-line depreciation has been charged on the basis of a 20-year life with estimated salvage value of $2,000 at the end of this life. The present book value is therefore $12,000.

The proposed replacement asset would cost $32,000 with an estimated physical life of 20 years and $2,000 salvage value at any age from 10 to 20 years. Replacement will not be made unless an economy study indicates that the proposed asset will pay for itself in not to exceed 10 years and also earn in addition more than a minimum return of 8 per cent per year on the average investment in the asset during the 10-year period. It is further assumed that operation and maintenance of the replacement asset will result in an annual saving of $4,200 per year.

In order to make the solution of the problem as simple as possible, it will be assumed that for the replacement to be economical the new asset must at least earn $3,000 per year for depreciation, so as to earn in 10 years the $30,000 additional investment ($32,000 for new machine less $2,000 salvage value of present machine), and in addition earn a return of at least slightly more than $1,200 per year on the average additional investment during the 10-year period (8 per cent of $15,000 average additional investment).

In the above example the annual cash savings (due to the new asset) of $4,200 per year in operation and maintenance charges will be completely offset by the extra annual investment charges on the new asset for depreciation and minimum satisfactory return on additional investment. It is, therefore, not economical to make the replacement, but on the basis of the data

given in the example, the present asset can hardly be expected to earn in the future any depreciation or other investment charges.

Depreciation and Taxes

It may easily happen that the conditions stated in this example may continue for another 10 years. In that case, under the present policy of the Bureau of Internal Revenue, $1,000 per year of depreciation would be charged off each year during the entire 20-year life of the present asset, and superficially it would seem that actual conditions had exactly followed the estimate on which the annual depreciation charges first had been established. But under the conditions of the problem the present asset is unlikely to be able to earn any depreciation whatever after the first 10 years, which means that if the total investment has not been returned to the owners in the first 10 years it will probably never be returned at all. Under present tax rates it would be possible for the owner of this asset to pay during the first ten years of the life of the asset a total of $8,550 in U. S. income taxes on what seemed to be profits but which was really only the recovery of the $10,000 in original investment represented by the amount by which depreciation allowances had been inadequate during the first ten years of life of the asset. The present 85.5 per cent corporation tax rate in the highest bracket is high enough to make the penalty on inadequate depreciation charges a very serious matter, and not even the present carry-back or carry-forward provisions of the law will give complete relief.

It may be argued that inadequate depreciation allowances in early years are compensated for by more than adequate depreciation allowances in later years. However, this does not mean that an overpayment of taxes in the early years will cause an equal reduction in taxes in later years. If there are no profits in later years, there will be no compensation for the overpayment of taxes in early years; this is true because the prepayment of taxes on what only seemed to be profits was merely the recovery of invested capital. If tax rates are lower in later years, the present high tax rates will have been applied on "excess profits" which are really not profits at all.

Determining Proper Depreciation Charges

I believe that past depreciation charges have been inadequate whenever the book value of an existing asset is higher than one could afford to pay for the existing asset in comparison with the most economical new substitute asset which might be purchased. An old asset may have many points of inferiority as compared with a new substitute asset. It will generally have shorter life expectancy. It may have higher current and prospective maintenance costs. Because of improvements in design the new asset may perform its function better and more economically than was ever possible with the old asset. Because of changes in service requirements that may have occurred since acquiring the old asset a new asset may be better adapted to the job to be done now and in the future. Particularly in the manufacturing industries the application of this criterion would often call for rapid write-offs in the early years of life. The application of this criterion would make depreciation charges on the books correspond more closely than at present to the write-offs assumed in engineering economy studies for proposed new investments. A more complete explanation of my ideas on this phase of the problem may be found in papers by Professor E. L. Grant of Stanford University and myself which have been published in the *Journal of Accountancy,* June, 1945, pages 451 to 455; *Transactions* of the American Society of Mechanical Engineers, July, 1942, pages 509 to 520; *Transactions* of the American Society of Civil Engineers, Vol. 108 (1943), pages 1242-1254, 1282-1284, and 1335-1342.

While the underlying theory is not particularly difficult or complicated, the complete application of the theory is hardly possible in actual practice. Fortunately there are many simple methods which can be used readily and which will give results that are sufficiently accurate for all practical purposes. The method that was actually used in the manufacturing industries prior to T.D. 4422 was really a pretty good method in that it charged off most of the investment of the average asset during those early years of the life of the asset when it was best able to earn its investment. The fact that the method used prior to 1942 was quite satisfactory in most cases was mostly an accident,

although it did often result from the innate conservatism of the business men of those days who generally preferred to "be on the safe side" by understanding current profits even where a saving in taxes was not of much consequence. With high tax rates the Government obviously cannot permit taxpayers to charge whatever rates they may desire, although I suspect a good argument might be made that any present reduction in taxes would be more than offset by the greater future taxes resulting from a healthier national economy. Also, as depreciation on an asset must stop for tax purposes when it is all charged off, even in individual cases lower present taxes may be expected to result in higher future taxes where depreciation charges in early years have actually been somewhat excessive. The best straight-line depreciation rate to use in any particular case would depend on the conditions existing in that case, but in general I suspect a satisfactory straight-line depreciation rate might be one that was 50 per cent greater than the rate corresponding to the full service life.

I have had no practical experience with the fixed percentage on diminishing balance method, but I have a feeling that this may be found to be the most desirable method to use, all things considered. Most persons seem to believe that this method is more complicated and more difficult than the straight-line method. I have reason to believe that, when properly handled, this method may be more simple and more easy to use than any other method that gives reasonably satisfactory results. But if this method is used the rate must, of course, be several times as great as the corresponding straight-line rate. The rates permitted by the Bureau of Internal Revenue for use with this method are definitely too low in most cases.

Depreciation and the Accountant

Cost accountants and certified public accountants naturally prefer to use depreciation methods that distribute capital investments through depreciation charges in ways that are both definite and uniform. The cost accountant seeks uniformity for the sake of facilitating cost comparisons between operations during different periods, while the certified public accountant seeks methods that are definite in order to protect him if his certification of the financial reports is questioned. As a former engineer and execu-

tive in mining and manufacturing industries, I also would prefer to use methods for calculating depreciation that were both definite and also uniform throughout the life of assets. Frankly, I do not believe that any such thing is at all possible, and I am convinced that accountants and all others who in any way come in contact with the depreciation problem must face the fact that depreciation is no more definite and uniform in its occurrence than are other items of indirect or overhead costs. It is, of course, situations of this sort that give cost accountants and certified public accountants the opportunity to show that they are more than mere bookkeepers.

It seems to me that it is very unfortunate that it is the tax aspects of the depreciation problem that receive the major attention of industrial managers, as well as their engineers and accountants. Under present and prospective high tax rates, the tax aspects must be given careful attention, but the economic and social aspects are also of very great importance. Recent proposals by important Washington officials that certain depreciation tax incentives should be offered industry indicate that these officials are beginning to realize that the present depreciation policy of the Bureau of Internal Revenue has certain undersirable results, but in my opinion, most such proposals do not strike at the real heart of the problem.

Summary

No one can say precisely what the solution is to a particular depreciation problem. After having devoted much thought to the problem for many years past, I am sure it deserves better handling than it has received from engineers, accountants, business men, or taxing authorities. An important thing, in my opinion, is for all of us to realize that the problem is fundamentally indeterminate and that there is no one right method that can be used safely in all cases; also that it is not possible to find even in any single case a depreciation method that is either definite or uniform over any length of time.

In general the rates permitted by the Bureau of Internal Revenue in the manufacturing industries are too low, but I also feel that the Bureau is entirely consistent in its practices and can hardly be converted to a policy of higher rates until engineers

and accountants undertake a complete rethinking of their own ideas concerning depreciation.

I believe that many situations exist in which the industrial economy will operate better if depreciation charges in the early years of the life of assets are considerably higher than is permissible under present income tax regulations, or under any system which uses as a standard of comparison straight-line depreciation accounting with rates based on the best evidence of average service life. I believe that it can be demonstrated that proposals for more rapid write-offs in early years may be sound in principle and not mere expedients to provide a tax incentive for investment; also that such rapid write-offs are as sound and as appropriate for existing assets as for those to be acquired in the future.

As long as income tax rates are high, business decisions will necessarily be made with one eye on the tax collector. Under current depreciation tax practices, the effect of this is to put a dangerous brake on the operation of our industrial economy. However, any single definite depreciation allowance of an arbitrary type, such as one-third in the first year and straight line thereafter, might have the effect of removing the brake in some instances but of applying an even more severe one in others. There is no single arbitrary plan that will necessarily lead to the results desired with regard to motivation of investment.

I believe that if systematic plans for writing off the cost of certain types of assets considerably more rapidly in the early years of life than is now permissible were accepted as correct in principle by the Government, industry, engineers, and accountants, the motivation aspect of the problem could be solved better than through any arbitrary tax incentive expedients.

TAKING THE PHYSICAL INVENTORY

**By W. B. Atchison, Jr., Staff Engineer,
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ONE of the basic responsibilities of management is to make accurate reports of the financial conditions and profits or losses of a company for the information and use of owners, stockholders, or creditors. In addition, such reports must reflect true income for tax purposes. The accuracy of financial statements depends to a great extent on the correctness of the count and the valuation of inventories on hand. Where there are no accounting records of inventories, or where there is no control over their accuracy, it is necessary to take a physical inventory at the close of the customary accounting periods of the year.

Advance Planning

Two major problems in taking a physical inventory are (1) that it is usually necessary to shut down the plant, and (2) that it is difficult to take an inventory that can be relied upon for accuracy. By advance planning and organization of effort, accurate inventories can be taken in one-third to one-half the time required for taking an inventory which has not been planned. It has been found that the most accurate and flexible technique in taking an inventory is through the use of tags with detachable coupons (Exhibit 2). As soon as the figures for the physical inventory are complete, they should be compared with the appropriate stock records.

Planning must be done for the inventory at least six to eight weeks in advance of the cut-off date. The organization should be set up and procedures and detailed instructions written and put in the hands of those responsible for the work. In addition, there should be at least two meetings of the entire organization —one, four to five weeks in advance of the inventory, to lay the groundwork, and another a few days before start of the work. In this way each person will be advised of his specific duties and responsibilities, and he will have ample opportunity to ask any questions.

The steps to be taken are in the following sequence:

1. Inventory organization and job duties.
2. Rough floor plans for locating storage areas.
3. Instructions to personnel.
4. Step-by-step procedure.

Inventory Organization

The first step is to determine the individuals who are to be part of the organization and to appoint an inventory supervisor. This individual must be one who has some prestige and authority in the organization as he will be charged with the responsibility for the complete physical inventory. He should not be burdened with the valuation procedure unless the organization is so small that he must handle both jobs. Each requires a different background and technique. A person who is usually good in organizing a group and arranging materials and counting the inventory is not so adept at pricing and summarizing for financial statements. The supervisor should have some accounting experience and be familiar in general with all materials used, the finished products, processes, and departments. He should also know the general location of all storage rooms and storage places. In the average sized organization it is not necessary to assign the full time of an executive to inventory duties throughout the year. He will be active in these functions only in the preparatory stages and at the time the physical inventory is taken. However, he should be constantly aware of problems that have arisen in previous inventories and should attempt to improve those conditions. A typical inventory organization chart is shown in Exhibit 1. The duties of the personnel involved are discussed below:

Inventory Supervisor

1. Has the full responsibility of counting, weighing, measuring, and estimating all materials and goods that are to be taken.
2. Makes up and issues the inventory organization chart which will show the names of the divisions and supervisory personnel. It will not be necessary to list names of the counters and tag writers. A statement as to the number to be used is sufficient.

PHYSICAL INVENTORY ORGANIZATION

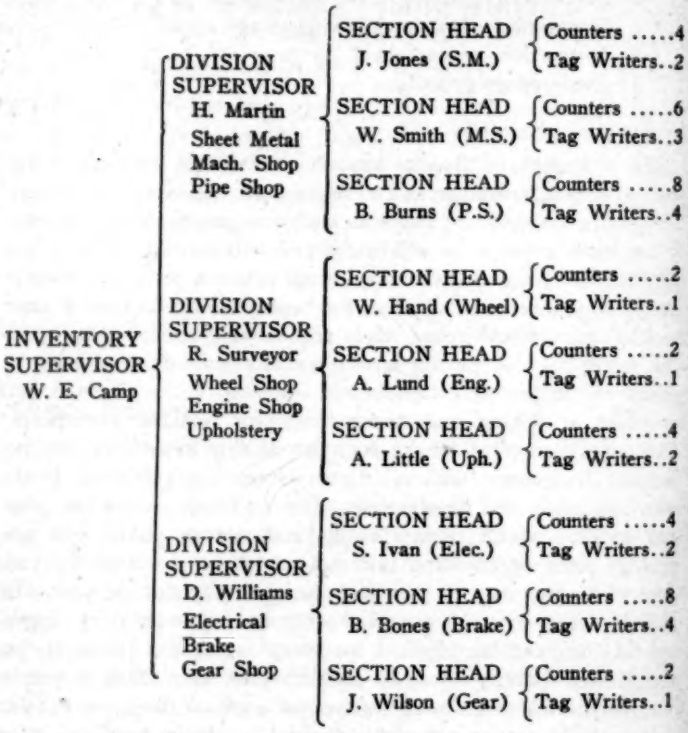

EXHIBIT 1

3. Has jurisdicition over these individuals only during the inventory preparation and taking period. They will report to him or to his delegated assistant.
4. Secures rough floor plans and layouts of the different sections of the factory. He will assign someone to lettering the divisions and numbering the sections.
5. Trains and instructs the division supervisors well in advance, and in turn, he may direct his division supervisors to instruct their own personnel.

6. Directs the issuing of inventory tags and sheets (sheets are used when tags are not practicable). He will also make out and issue tag tally sheets which are used for entering the tag numbers and divisions to which they are issued.
7. It is his responsibility to see that all tags are accounted for. In large organizations, he may want to delegate these functions, or parts thereof, to an assistant.
8. Makes a tour through some of the largest and most active departments after the coupons have been removed. This is a final check to see that all items are tagged.

Division Supervisor

The person should be one who is familiar with materials and has a general knowledge of departmental and stockroom locations. He can be a senior storeskeeper in charge of various classes of stock. In some cases it is preferable to have persons from the accounting department who have been working on material control, when storeskeepers are not available. The duties of a division supervisor are:

1. Reports directly to the inventory supervisor. He may have charge of one department or several departments. This delegation will be known as his division.
2. Issues all tags and instructions, both oral and written, to his section heads.
3. Holds meetings with his section heads to explain the instructions.
4. Receives all inventory tags and sheets, and turns them in with the tag tally sheets to the inventory supervisor.
5. After the inventory is completed, he will make a tour of inspection through his department to see that all items have been tagged.
6. All questionable cases as to the quantity and quality of goods within his division will be called to his attention for decision.

Section Heads

There may be one or several section heads coming under the jurisdiction of a division supervisor. These preferably should be sub-foremen or lead men from the departments in which the

inventory is to be taken. They should be the type of foremen who have proved to management that they know processes and materials. Their duties will be as follows:

1. Will have direct supervision over the tag writers and counters in their particular section.
2. Will be responsible for the instruction of their personnel, and for selecting the number they need.
3. Will supervise the preparation of their section of the department, putting stock in order, and identifying goods which bear no label or other means of identification.
4. Will be sure that all goods are in condition to be counted or described.

Duties of a Counter

He should be selected from the section in which he is to take the inventory. He should be a person who has been with the company for some time and has a fair knowledge of the processes and stocks. He will count, weigh, measure, and identify all stock in his section. He will call out this information to the tag writers who are the balance of the team.

Duties of a Tag Writer

This person should also be an indiivdual from the department or section that is being inventoried. He will write in all the pertinent information required on the tag (Exhibit 2). He also assists the counter whenever necessary.

Rough Floor Plans for Locating Storage Areas

The inventory supervisor must secure rough floor plans or schematic layouts of all locations that are to be inventoried. He will work with the division supervisors in assigning the divisions. A division will be lettered and may include one or more departments, thus:

Division "A" { Sheet Metal Department
Machine Shop
Pipe Shop

The division letter will be entered on the lower right-hand column of the drawing.

No. 6002 Date 12/31/45
Dept. Machine Shop
Part No. CN 148-54
Part Name Cylinder
Condition O. K.
Quantity 12

No. 6002 Date 12/31/45
Dept. Mach. Shop Sect. 6
Part No. CN 148-54
Name Brake Cylinder
Condition O. K.
Quantity 12
Unit Ea. Unit Cost $5.00
Total Value $60.00

Last Operation: No.
Drill and Tap 4
Next Operation: No.
Bore Grinding 5

Initial Below

Count	Writer	Sup'r	Price	Ext. Ck.
B.B.	W.C.	B.C.	A.B.	C.D.
Check Count			Ext. E.H.	Ent'd B.A.

Form No. 12 INVENTORY TAG

EXHIBIT 2

Each division head will assign one or two departments, depending upon size, to a section head and together with the section head will assign section numbers to the departments. These letters and numbers are primarily for the division of territory among the inventory personnel. Each group must therefore know the assignment ahead of time.

Instructions

The Inventory supervisor and the division supervisors will use the inventory manual for basic instruction. Section heads receive a notice of inventory containing the proper instructions. Other instructions are presented below.

General Instructions

All goods must be arranged so that they can be counted easily and in such a manner that labels or indentification tags are facing outward. They should be in uniform piles and rows. All materials must be placed in plain sight. Every piece of material should be marked or labeled for identification purposes.

Instructions to Accounting Personnel

Care must be taken to make a distinct cut-off between goods already in the receiving department and goods received after the inventory has started. Items received before the inventory is taken should be entered on the stock record cards.

The same procedure will apply to sales. In cases where there are continual receipts and shipments that cannot be held up for inventory purposes, it is best to mark off a separate location where this stock can be piled and lettered: "Billed," "Unbilled," "Invoiced," or "Not Invoiced."

Instructions to Counters

Everything in the section must be weighed, counted, or measured. In counting it may help to count small pieces from one container, placing them in another during the process in order to avoid duplication.

When items are very small and numerous, it is best to use a counting scale for a weigh-count. In measuring liquids, the measuring stick should be absolutely vertical when being lowered

into the tank. The reading is taken at the bottom of the ellipsis made by the liquid mark. Charts of tank calibrations can then be used to find the volume on hand. If no such charts are available, the following formula is used:

(Height of liquid on stick x Pi) x (the radius of the tanks)^2.

Coal and chemicals in piles should be estimated by persons using them and reconciled against book balances. If there is a large discrepancy between the book and physical quantity, then the total physical lot inventoried should be tagged or marked and kept separate and distinct from all other incoming lots. The inventoried lot should be used first, and when it is completely gone, this information with the date will be written on the inventory tag and sent to the Accounting Department for adjustment.

Instructions to Tag Writers

All the tags should be predated with a rubber stamp, and if there are a great many for a particular department, the name can also be stamped or typed in. The following items should be filled in on the stub and the coupon:

Part Number	The number which appears on the item.
Part Name	The name that is familiar to all departments.
Condition	Whether the stock is a reject or has some defect in it.
Quantity	Quantity on hand at that location at that particular time.
Last Operation, Name and Number	The last operation that had been performed on the part.
Next Operation	The next operation to which the part is scheduled.

The writer will then initial in the spaces at the bottom of the tag. He will also fill in the initials of the counters and will then hand the tag to the counter to be placed on the parts or materials.

Inventory sheets (Exhibit 4) are used when there are a great number of different single units to be inventoried in one area. The inventory tags would not be practicable, and it will be easier

to list each unit on a sheet; as soon as it is listed, attach a gummed label, cross-referencing it to the sheet.

Step-by-Step Procedure

The *Inventory Supervisor* will issue inventory tags and inventory sheets (Exhibits 2 and 4) that have been predated. The number to be issued can be determined by conference with the section heads and will be based on their estimate as to the number they need or the number they used on the last inventory. He will give these to the division supervisor.

He will also make up two copies of a tag tally sheet (Exhibit 4) on which are entered the tag numbers charged against the division supervisors and also the division and department to which they are assigned. These tags will be given out one week in advance. A carbon copy of the tag tally will remain with the inventory supervisor; the original will go, with the tags, to the division supervisor.

The *Division Supervisor* will receive the tag tally sheet and inventory tags. He will check to see that he has all the tags charged to him and that he has a sufficient number of the types of tags and sheets that he needs for raw materials, work in process, finished goods, and supplies.

He will then confer with his section heads one week in advance, at which time he will give them a notice of physical inventory (Exhibit 3) which constitutes their instructions, and he will also check at the same time to see that he has enough tags for distribution to his counters and tag writers. At this time he will give out the tags and inventory sheets to the section heads and enter the numbers issued and the section to which they are charged.

Note: All tags must be returned or accounted for whether they are used, voided, or unused.

The *Section Head,* upon receipt of the tags, will make out the ones for stock that will not move until after inventory time. In doing this, he will save time on inventory day for only the active stocks. This is an important time-saving step and must be carefully considered. In one concern it was found that 30 per cent of the materials and finished goods on the floor and in the stockrooms were not scheduled for production and shipping until several days

NOTICE OF PHYSICAL INVENTORY

To be taken at the close of business in.....
Department on .....Date .....Time.

Know what you are to inventory and where you are to start. If you are not sure, check with your immediate supervisor. Collect your personnel for last-minute instructions or questions before starting.

..... will be in charge of the inventory in section ..... and will be responsible to .....

Please make the following preparations and advise Mr. ....when they are completed:

1. Select experienced and reliable operators for your personnel.
2. Have them get all work places in order well in advance.
3. Arrange, stack, segregate all stock so it is easily identified and counted.
4. Requisition only enough material to start the next shift after inventory. In doing this, there will be a minimum of stock on the floor.
5. Routine instructions are attached for your counters and tag writers. These are to be given out as soon as you select them for the job.
6. Have a short meeting for the counters and the writers two or three days in advance for any questions they might have. Read over the instructions to them.
7. All tags or coupons must be accounted for.
8. All raw materials, work in process, finished goods, and operating supplies in your section must be inventoried by you and your group.
9. The attached inventory tag is to be used wherever possible. If there are many single units, tags would be impracticable; use the inventory sheet attached.
10. Your tags will be colored ..... and can be obtained from Mr. ....., division supervisor.
11. After your section has been tagged and the coupons have been removed turn them in with the tag tally sheet to Mr. ....., division supervisor.
12. Mr. ..... will be your checker.

Signed .....
Inventory Supervisor

EXHIBIT 3

SHEET NO. 1028 DEPT. Machine Shop SECTION A DATE 12-31-44

PT. NO.	NAME	QTY	LAST OPERATION	UNIT	UNIT COST	TOTAL VALUE
D124671	GENERATOR	1	Assembly	Ea.	10.00	10.00
DC123895	ENGINE SHIELD	1	Plate	Ea.	2.00	2.00
DC12844	SPUR GEAR	1	Heat Treat	Ea.	5.00	5.00

COUNTER | WRITER | SUPV'S'R | PRICED | EXTENDED | EXT. CHECK | ENTERED

INVENTORY SHEET

EXHIBIT 4

after the inventory. The balance of tags will not be issued until the start of inventory day.

The *Tag Writer* receives the tags and at the appointed time will go with the counter to take the actual inventory. The counter will be expected to call out the information to be filled in on the tag, and if it is not called out, the tag writer will ask for it. He will fill in the following:

1. Location, department, and section.
2. Part number and name.
3. Brief description, if necessary.
4. Quantity.
5. The last operation, name and number, performed on the article.
6. The next operation, name and number, to be performed.
7. Condition of the stock—defective, rejected, etc.
8. Initials of the counter.
9. Initials of the writer.

In the case of long counts, the tag writer who goes along with the counter will help count in order to speed up the operation.

The counter and tag writer must take a starting point by location and work to a finishing point by location. The inventory should not be taken by stock classification. In taking it progressively by location it can readily be seen just how much has been inventoried and how much remains to be done, as the inventoried part will be covered with tags.

After the tag has been filled in, in two parts, the writer will hand it to the counter, who will attach it to the parts or materials.

The Counter should place the tag in a conspicuous spot. If possible, it should be placed on the bottom or last piece of the parts; then after all of the inventoried lot has been issued or consumed, the tag can be turned in as a notice that the lot has been consumed. In such case it would be sent to the production clerk, who would stamp it, "All Issued," and then send it to the accounting Division for a check of their records of consumption. This would mean that that lot would have to be kept separate from new lots coming in. Many times this is a desirable check, both to see that the physical inventory is correct and to keep the stock records in balance.

The *Section Supervisor and/or Checker* will go to those sections of the department which have been inventoried to remove the coupons from the tags. As he lifts the coupons he will make a spot check for count, part number and description, last operation, etc. After all the coupons have been removed in a section, he will send them to the division supervisor.

The *Division Supervisor* will check the coupons returned against his tag tally sheet in making an accounting for each tag issued. As soon as all tags have been received, he will make a jog beside the entry and place his initials on the sheet. He will send the coupons to the inventory supervisor. When his entire division is completed, he will send the tag tally sheet to the inventory supervisor.

The *Inventory Supervisor* will receive the coupons and sheets, and either he or a delegated person will check them for completeness and accuracy and send them to a clerk for sorting.

The *Sorting Clerk* will sort the coupons according to:

1. Raw material by item as a separate class.
2. Work in process, first by item, and second, progress of item through manufacture, i.e., items having least amount of work completed, filed in front.
3. Finished goods by item and general classification.

The clerk will separate each of these three divisions and send them to the stock records clerk for pricing.

The *Stock Record Clerk* will receive the coupons and price them according to the company policy. After pricing, the stock record clerk sends the coupons to the comptometer operator. (From this point on, it would be desirable to organize the work groups by classes of stock or departments, whichever is best, possibly the same as the inventory organization. Those people most familiar with certain kinds of stock can work faster and more accurately.)

The *Comptometer Operator* will extend the coupons and give them to the inventory typist.

The *Inventory Typist* will type the tags on the inventory summary sheet (Exhibit 5). She will type the following: tag number, part number, name and description, quantity, cost per unit, and extension.

The typist will leave enough room at the bottom of each differ-

CLASS OF STOCK WORK IN PROCESS - LANDING GEAR EQUIPMENT
INVENTORY DATE 12/31/44

SHEET NO. 22

LOCATION DEPT.	LOCATION SECT.	TAG NO.	PART NO	PART NAME	LAST OPER NO.	QUANTITY	PER	COST	PER	EXTENSION
M.S.	1	6000	CM 143-54	Brake Cyl.	3	18	ea.	4.00		72.00
	2	6001	"	" "	3	10	ea.	4.00		40.00
	4	6002	"	" "	3	5	ea.	4.00		20.00
		6003								
	6	6004	"	" "	4	12	ea.	5.00	ea.	60.00
										192.00

INVENTORY SUMMARY

EXHIBIT 5

ent item and classification for subtotaling. She will give the sheets and the coupons to a checker.

The *Checker* will check each coupon against the entry on the summary sheet to see that all the data thereon are entered in the appropriate columns and that all coupons have been entered on the sheets. She will foot the columns and turn the sheets over to the comptometer operator who will check her footings.

Miscellaneous

After the inventory has been taken, the division supervisor will walk through all sections under his jurisdiction to see that each item has a stub attached and to see that all coupons have been lifted.

White tags can be used for customers' goods. These should be inventoried the same as regular stock. If work has been performed, they must be priced for the labor and overhead costs.

In cases of inventory for valuable goods, an outside auditor may be called in for count or spotcheck.

A Gantt chart can be used for scheduling all phases of the inventory and will be kept by a clerk in the inventory supervisor's office. (Exhibit 6).

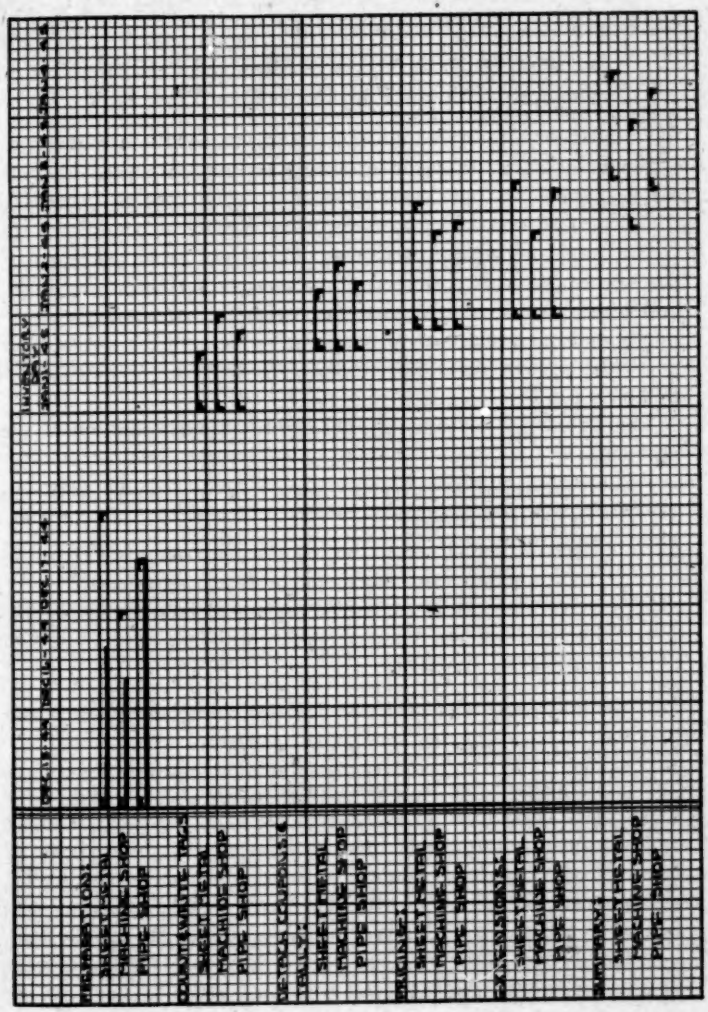
INVENTORY PLANNING CHART
PURCHASES
SALES
PURCHASES
SALES
PURCHASES
SALES
PURCHASES
SALES

Exhibit 6

STANDARDS—CAN THEY BE SWALLOWED WHOLE?

By W. I. McNeill, Vice President and Controller, General Aniline & Film Corp., New York, N. Y.

THERE have been many articles published on the use of standards for accounting and operating control purposes. In these articles, standards have been advertised to industry as furnishing a short-cut to accounting and operating control at a minimum of clerical cost and with a maximum of control. Some adherents of the use of standard costs—with variances—for materials, labor, and overhead are positive that the mellenium in accounting simplicity and operating control is attainable through the use of their particular system regardless of the type of business or the conditions.

The following questions are pertinent to a consideration of the problem:

1. Can standard costs be applied to, and digested by, all types of business?
2. Should actual costs be eliminated completely, for all types of business, when standards are introduced?
3. Are there some circumstances where both standards and actuals can live together happily with each serving its own particular function?

It is the purpose of this article to consider these points.

Universal Applicability

The enthusiasm that is sometimes generated for the application of standard costs to all types of business has a counterpart in the enthusiasm of some people for a definite kind of remedy for all types of ailments. For instance, we have homeopathy, osteopathy, chiropractic, Christian Science, etc. Some people resort to osteopathy as a cure for all kinds of ailments; others are equally positive that homeopathic treatment is the only cure for the average physical disability. Chiropractic treatment and Christian Science methods appeal with equal force to adherents of each as the one and only remedy. As a matter of fact, each has its place, and it is a matter of judgment to decide which method fits the particular

ailment with which a person may be confronted. Similarly, standards have their place, and it becomes a matter of judgment to determine the degree to which their use may be of value.

There is little need to expound on the detailed technique for the use of standards for accounting purposes inasmuch as the subject has been adequately covered in accounting literature for the past several years. It will suffice to say that standards may be applied to materials, labor, and overhead, and the variances from actual may be shown by groups of expense or departments according to the needs of the particular plant. Also, in this discussion it is assumed that wherever standards are used, they have been scientifically prepared.

Significance of Variances for Control Purposes

From the point of view of accounting alone, there are only two considerations necessary in deciding upon the use of standard costs. First, will inventories be properly priced, and, second, will standard net profit data by product be sufficiently accurate to tell the company whether or not it is continuing to make money on each product. From the point of view of operating control, however, the problem is somewhat more complicated. The average standard cost accounting system with variances for materials, labor, and overhead does not provide the operating department with detailed control data and forces it to set up separate control records for its own use. This may be illustrated to some degree by the use of standards which one finds in the game of golf.

When a golfer starts out for a game, he usually takes with him a score card showing what is considered par for each of the eighteen holes and what is total par for the course. Spaces are provided in which the actual score for each hole may be recorded. After playing a given hole, the actual score is recorded and a comparison made with par for that hole. During the game, there may be some holes played under par and some considerably over par (the author's weakness). At the end of the game the total score for all holes is usually compared with the total par for the course, but the variance between total score and total par has minor significance unless you can look back over the score and find out the holes on which performance was good and those on which it was bad. It is possible for good golfers to have very little variation from par

in total and yet be very bad on one or more holes which perhaps has been offset by "birdies" on other holes. The real value of the score card is the opportunity it gives for analysis of the results over several games played on the course and to work on the individual holes which seem to cause the most trouble. In this way the over-all score is improved. If this procedure were not followed and the golfer had simply a little adding machine on which to punch the score on each hole so that he would have a total for the 18 holes to compare against par for the course, this figure, or total variance, would do him very little good, unless his memory was long and he was able to remember for several games the holes on which his performance was better than average and those on which his performance was poor.

This same logic may be applied to factory control of operations in a department or plant which has a number of operations and a number of different products. The total variance for the entire department in any one of the cost elements is of as much value to the foreman of the department for control purposes as the comparison of total golf score to total par for the course is to the golfer without keeping a detailed score card.

Setting Standards Based on Actual Cost Studies

In view of the above comments, it seems desirable, in all but the very simplest of mechanical businesses, to provide in the accounting system some means for furnishing the factory with useful operating control data. For the sake of illustration, assume that the factory which you are considering has never had scientifically determined standards and does not have a cost system in operation which gives actual costs within a reasonable degree of accuracy. (In defining what is meant by reasonable degree of accuracy, we might say that plus or minus 5 per cent may be considered reasonable for accounting and factory control purposes.) In the absence of standard or actual costs, the first job is naturally to get actual costs because a person cannot very well tell what a standard should be until he has facts over a long enough period of time to know what variables actually occur. The problem of cost determination involves departmentalizing the plant, establishing labor records by product and operation, and determining the use of materials by product and operation with yields, scrap, losses, degradings, etc.

After actual costs have been determined for a long enough time to enable everyone to know what variables may be expected from month to month and what unusual conditions are likely to be met, the problem of deriving standards can proceed much more intelligently. Ordinarily one cannot be sure of all possible variables unless actual costs are obtained for at least a year.

During this time, the industrial enginering department can be busy assemblying data for labor and other standards by operation and by product. In certain factories there may be some labor which varies with volume and other labor that is fixed. Effect should be given to these differences in the standard cost that is set. Standard overhead costs can be set up for fixed and variable expenses in any process center or department.

When standard costs have been set for one or more departments, the accounting department and the factory can begin to use them in comparing actual results with standard. This can be done from day to day, if necessary, without the use of money. For instance, the comparison of actual with standard (man hours for labor, or machine hours on burden) can be made as extensive or as restricted as the demands of operating control dictate. If a comparison of standard labor and overhead dollars with actual dollars at the end of the month is significant, such a comparison can be made.

Elimination of Actual Costs?

After actual cost data has been compared with standards over a period of time, a decision should be made by the company whether to continue the determination of actual costs or whether the elimination of detailed records and the determination of over-all variances for given departments will suffice. In some cases, the variables of operation are such that an over-all variance will never give the degree of operating control that is necessary. In other cases where the operations are well standardized and mainly mechanical, it may be possible to eliminate actual costs because variables in operation are so unlikely that an over-all control is sufficient for the factory. In such cases, a net profit determined on the basis of standards is not likely to be far enough from actual at any time to cause difficulty in making business judgments. It is not necessary for a plant to be wholly on a standard cost basis

or wholly on an actual cost basis. It is quite possible that the continued use of standards and actuals may be of value in certain departments and not in others. In the final analysis, the net effect on the profits of the company over a period of time will be the determining factor in deciding whether or not the amount of control that is used pays for itself.

In considering the standards problem, one should have in mind the difficulty of analysis and control in case actual costs are eliminated. It may take more and higher caliber clerical effort to analyze variances than it would to get the complete actual costs in the first place. This again becomes a matter of judgment. It may be said, however, with certainty, that in a plant where the operation is other than the most simple mechanical type, it is rarely ever true that proper control can be obtained in the beginning, simply by the use of standards and without keeping actuals for at least a year.

The conclusion which may be derived from the above discussion is that standards, like any kind of medical treatment, have their place. One must realize that there is a time and place for everything and the degree to which standards or actuals are used, singly or together, will depend on the particular conditions to be met in both the accounting and operating divisions of the business.

Walter A. Staub
1881 - 1945

His many friends were saddened to learn of the death on November 5 of Walter A. Staub, Partner of Lybrand, Ross Bros. & Montgomery, at the age of sixty-four. Born in Philadelphia, and educated at Girard College, Mr. Staub joined Lybrand, Ross Bros. & Montgomery soon after his graduation and became a partner of the firm in 1911. During 1933 and 1934 he served as President of the New York State Society of Certified Public Accountants, and for the past several years has been Chairman of the Committee on Accounting Procedure of the American Institute of Accountants. The author of several books and numerous articles on accounting and taxes, and a frequent speaker at gatherings of accountants, Mr. Staub will be remembered by N. A. C. A. members for his outstanding talk on "Wartime Problems in the Presentation of Financial Statements" at the 1943 International Cost Conference in Boston.

OUR OPEN FORUM

This section of the Bulletin is available to all for the informal discussion of technical matters of interest to our members. Included here will be comments on articles, ideas, and suggestions arising out of these articles, and other correspondence in which our members are likely to be interested. The ideas expressed are those of the individual correspondents, and all shades of opinion will be welcomed to the extent that the ideas expressed are constructive and of general interest.

Installing a Punched-Card System

Editor, N. C. C. A. Bulletin:

I have read Troy A. Chapin's article in the October 1, 1945, *Bulletin* and would like to recommend it as a guide for new installations as well as for the improvement of presently established punched-card systems.

The all-important section on proof controls is quite comprehensive, but to be effective it is necessary to establish proper cross reference between the original source record and punched cards. This cross reference provides the means of readily checking back second or subsequent distributions if they do not check to control totals. For audit purposes and internal use, we have found that properly controlled and cross-referenced punched cards are the fastest and most accurate means of checking back multiple distributions.

The training and selection of tabulating department personnel is very important, and I would like to add that the production tempo of a department is determined in the initial selection of personnel. Presently employed personnel should be used wherever feasible, but an experienced key punch operator should be hired, if possible, as a pace setter. Temporary experienced help can often accomplish this purpose.

The section on "Scope of Application" is excellent but leaves the impression that single distribution applications can be performed in less time normally. The determination of whether a single distribution is a tabulating application is often dependent upon what percentage of information can be prepunched or duplicated and the volume involved. The prepunched application is the fastest and the most accurate of any tabulating application and can be used in many single distribution jobs.

I would like to add that in planning a new installation, rotation of work should be considered and put into effect as soon as possible to guarantee efficient operation regardless of sickness, separation, or vacations.

George J. Maly,
Milwaukee Chapter.

Editor, N. A. C. A. Bulletin:

Troy A. Chapin's article in the October 1 issue of the *Bulletin* thoroughly

covers the problems incident to the installation of a punched-card accounting system. However, there is one point which he did not touch upon. Possibly, it did not arise in that particular installation. It concerns the conditioning of minor accounting as well as supervisory personnel to the acceptance of a change. An efficient punched-card accounting system brings about an integration of accounting procedures and centralization of responsibility, particularly in small companies. This together with the resultant reduction and shifting of personnel often induces an antagonistic attitude on the part of some of the employees not directly responsible for the installation. As Mr. Chapin has suggested, department heads should be brought into a committee to set up procedures and take an active part in the change-over. This, of course, is essential, but there may be men in these departments who have been posting their ledgers for twenty years and may be reluctant to lay aside their "quill pen and eyeshade" for any new-fangled machine.

The educational program should go all the way, not necessarily to include the actual operation of the machines, but each accounting employee should be made to feel that his cooperation and interest will be required in the change-over, and that his job will be just as secure, and his value to the company just as essential under the new system as under the old. Personnel reductions may be effected, but usually not beyond a normal turnover so that no conscientious employee need be concerned about his future status.

Although these adjustments are eventually made, an initial and thorough explanation of punched-card accounting to all personnel would contribute much to a smoother change-over.

J. E. Starkey,
Denver Chapter.

Accounting Control of Incoming Material

Editor, N. A. C. A. Bulletin:

With respect to the article by Harry C. Anderson (*N. A. C. A. Bulletin*, September 1, 1945) it is the writer's opinion that in cases where all incoming materials are to be inspected, the preparation and presentation of the receiving report and other accounting papers as to damage, loss of materials in transit, or variance from purchase orders as to quantity, weight or specifications, should be the duty of the receiving inspection department or section. This leaves to the receiving clerks the unloading of the materials, listing the shipments on a receiving sheet prepared in duplicate, showing number of boxes, cartons, cases, etc. The duplicate receiving sheet is forwarded with the material to the inspection department or group, and the original is filed for reference.

The above paragraph is not to be construed as a criticism of an excellent thesis but as a method of segregating material as to standard, damaged, or substandard at the source. In turn this prevents delivering inferior materials to processes, machines, and stockrooms and also prevents possible

future adjustments and corrections of data received by the various interrelated departments.

WALDO ROTHERT, JR.,
Los Angeles Chapter.

ACCOUNTING EFFICIENCIES IN SMALL COMPANIES

Editor, N. A. C. A. Bulletin:

I have read with interest Glenn R. Kleinau's article in the October 15 *Bulletin*. There is no doubt that one finds many inefficiencies in small offices where the owners keep the records and have very little knowledge of bookkeeping. You can, however, keep these records in a more practical manner than that described. For instance, in place of using a big ring book to keep the records of various accounts, you can use a large legal size folder, with paper fasteners, and insert accountants' work sheets (13 column or less). In this way one can keep the records separate, a folder for each record, such as, Balance Sheet, Inventory, Manufacturing Expense, Operating Statement, Administrative Expense, etc. This would be more flexible and less cumbersome. When you are working on one particular record, you do not have to handle a large ring book, but keep each record separate in a folder, and these, in turn, are filed alphabetically in a steel file cabinet which can be locked. The accounts, of course, all balance with the control accounts in the General Ledger. Should an error occur, it would not be difficult to find, since the accounts are segregated and can readily be checked with the General Ledger Control. After the accounts have all been posted for the month, a balance sheet and operating statement can usually be made up in a day.

C. J. STEITZ,
Akron Chapter.

EXPENSE AND PROFIT ALLOWANCE ON INVENTORIES RETAINED IN TERMINATED CONTRACTS

Editor, N. A. C. A. Bulletin:

It is my understanding that some contractors are not taking advantage of their rights with respect to reimbursement for general and administrative expense and profit on inventories retained by them in connection with terminated contracts. If this is the result of a decision on the part of the contractor, then it is all to the good. For example, if in the negotiations the contractor was able to retain his inventory at a favorable price, it is understandable that he might not care to push for every penny of reimbursable cost. Any negotiation involves a certain amount of give and take and breaks down if both parties insist upon adhering strictly to their legal rights, especially in connection with costs where judgment, opinion, and convention all play a part. If, on the other hand, the contractor does not enter a claim for these costs because he does not realize that he is entitled to them, or because some termination officer has mistakenly told him that he is not entitled to them, it is unfortunate for the contractor.

In accordance with the Contract Settlement Act of 1944 the contractor at termination is entitled to compensation for costs incurred which are reasonably necessary for the performance of the war contract and properly allocable to the terminated portion thereof, plus such allowance for profit as is reasonable under the circumstances Further, the Uniform Termination Article provides, in the event of a formula settlement, for reimbursement of costs and for profit at stated percentages. In both cases the costs and profit are allowable without reference to the retention of any part of the inventory by the contractor.

The Joint Termination Regulation, Section IX—Forms and Instructions, presents a specimen proposal on Form 1 with supporting schedules. It will be noted in the example given that the proposed settlement lists the inventories at cost, as well as dies, jigs, and other costs, and to the sum of all of these items a rate is applied to arrive at the general and administrative expenses in the proposal. The G. & A. so computed is then added to the previous items, and a rate is applied to the total to arrive at the profit in the proposal. The item of disposal credits, representing in part the contractor's retention offer, appears on line 18 and has no bearing on the G. & A. or profit entered above.

Thus the Act, the Uniform Termination Article, and the specimen proposal provide for reimbursement of general and administrative expenses properly allocable to all of the terminated portion of the contract without regard to inventories retained. The contractor may for one reason or another decide not to claim G. & A. or handling costs on inventories retained, but this should be a definite decision on his part and not a matter that was overlooked.

C. B. Nickerson,
Boston Chapter.

COST CURRENTS

Corporate Taxes Changed in Revenue Act of 1945—The recently enacted Revenue Act of 1945 makes the following principal changes in corporate income and excess profits taxes:

1. Repeal of excess profits taxes.
2. Repeal of capital stock tax.
3. Repeal of declared value excess profits tax.
4. Reduction in surtax rates.

The repeal of the excess profits tax is effective for years beginning after December 31, 1945. In the case of a fiscal year beginning in 1945 and ending in 1946, the tax is applicable only to that portion of the fiscal period ending with the above date. The unused excess profits credit carryover is also abolished. The carryback, however, has been retained in the law through 1946. Therefore it will still be necessary to compute the excess profits

credit for 1946 in order to obtain a carryback to 1944 and 1945.

The capital stock tax is repealed for years ending after June 30, 1945.

The declared value excess profits tax is repealed with respect to income tax taxable years ending after June 30, 1946.

The normal tax rate is unchanged, but the surtax rate is reduced from 16 per cent to 14 per cent in those cases where surtax net income exceeds $50,000, and a reduction from 10 per cent to 6 per cent on the first $25,000 of surtax net income in those cases where this net income does not exceed $50,000. These changes are also effective beginning in 1946, and a company having a fiscal year beginning in 1945 and ending in 1946 will compute its tax for the fiscal year under both laws.

Procedure for Obtaining Renegotiation Rebates—A contractor who has refunded excessive profits under the Renegotiation Act will be entitled to a renegotiation rebate for each fiscal year where refunds were made if he elects to accelerate the amortization of his emergency facilities pursuant either to a non-necessity certificate or to the Presidential Proclamation of September 29, 1945. The rebate will be in the amount of the increase in the amortization deduction, less the corresponding decrease in income and excess profits taxes. The contractor must first apply to the Bureau of Internal Revenue for a recomputation of his tax liability for each year involved. A rebate claim must then be filed with the War Contracts Price Adjustment Board, Washington, D. C., for each year. The claim form, which is given below, must be accompanied by the Revenue Bureau's recomputation of taxes and by Schedule A. The claim form is as follows:

War Contracts Price Adjustment Board
Room 3D 573, The Pentagon
Washington 25, D. C.

In accordance with (Agreement No. .....) (or Order) dated ..... executed on behalf of the United States by the..... and determining ex-
Title of Executing Officer
cessive profits pursuant to the Renegotiation Act, the undersigned has eliminated $..... of excessive profits for its fiscal year ended. .....

Upon a recomputation of the amortization deduction pursuant to section 124 (d) of the Internal Revenue Code in connection with the determination of the Federal taxes of the undersigned for said fiscal year there was an increase of $..... in total amount of the amortization deduction for said year.

The undersigned therefore claims a net renegotiation rebate for said fiscal year in accordance with subsection (a) (4) (D) of the Renegotiation Act, and the regulations promulgated thereunder by the War Contracts Price Adjustment Board and in support of such claim submits herewith the following documents:

1. Statement by the office of the Commissioner of Internal Revenue

of Recomputation under section 124(d) of the Internal Revenue Code;

2. Schedule A in the form set forth in paragraph 736.2 of the Renegotiation regulations.

.....
Name of Contractor

By.....
Title of Authorized Official

* Certification

I hereby certify that the facts herein set forth above or appended are true and correct to the best of my knowledge, information, and belief and that in my opinion the claim hereinabove made is meritorious.

....
Date Signature of Person Executing Claim

Schedule A which must accompany the claim calls for detailed information covering the history of the facilities and the related amortization deductions.

It should be noted that the gross renegotiation rebate (before reduction for taxes) cannot exceed the amount of the original refund of excessive profits.

Excess Profits Tax Refunds To Be Paid in January—It is reported that the Treasury Department will make payments in January, 1946, covering taxpayers' postwar refund credits under the excess profits tax. The refund bonds must be assigned to the Secretary of the Treasury in the presence of authorized witnesses. The latter include notaries public and executive officers of banks and trust companies. It is expected that the redemption will amount to $1,300,000,000, and the bondholders are urged to turn the bonds in immediately in order to insure prompt redemption after January 1, 1946.

Comment on Example Cited in Recent Bulletin Article "The Tax Adjustment Act of 1945"—A recent communication from an N. A. C. A. member concerns the timely article "The Tax Adjustment Act of 1945" by Harvey W. Peters which appeared in the October 15 *Bulletin*. The reference is to the example presented on pages 140 and 141 illustrating the extension of the time for paying the prior year's tax because of an anticipated loss or unused excess profits credit carryback. The wording of the example and comments may be interpreted as indicating that the extension of the time for payment of the preceding year's tax liability (the year ending September 30, 1945) is permissible only if that year's income is reduced by the carryback from 1946. Such interpretation would be erroneous and probably was not intended by the author. Actually the relief would be available on the basis of a reduction in income for the earlier year (the year ending September 30, 1944) which would be the first carryback year. Since carry-

backs must first be taken to the second preceding year, any other interpretation would make the relief provision meaningless in many cases.

ASSOCIATION NEWS

The New England Regional Conference

The first postwar regional meeting of the Association, a New England Regional Conference, sponsored by the Worcester Chapter, was held at the Sheraton Hotel, Worcester, on November 2. The evening before the conference was given over to a chapter officers' conference, attended by 50 chapter and national officers and directors and devoted to the consideration of chapter operation.

At the morning session of the conference, Stanley Z. Bronner of the Bridgeport Brass Co. spoke on "Forecasting for Sales and Production Budgets," and National Director Clinton W. Bennett of Cooley & Marvin on "Cost Determination for Pricing Purposes." Edwin A. McConnell, Controller of Norton Co. and President of the Controllers Institute, addressed the luncheon meeting on "The Accountant's Job in the Postwar Period."

The afternoon session was devoted to a discussion of "Analysis of Selling and Distribution Costs" by Robert N. Wallis of the Dennison Mfg. Co. and of "Cost Control or Catastrophe" by Percy L. Proctor of Titeflex, Inc. Mr. Proctor's talk was broadcast by the Yankee Network covering all New England. The conference ended with a banquet and ball at which Henry C. Perry, Treasurer of Heywood-Wakefield Co., presided as toastmaster.

A vote of thanks is due the Worcester Chapter, and the members of the Conference Committee, for the planning and conduct of this most worthwhile conference. The conference was under the general chairmanship of Kenneth H. Bergstrom, with the following serving as committee members: Everett M. Hicks, Program; Charles A. Forster, Finance; George D. Crosier, Entertainment; Robert B. Service, Jr.; and G. Myron Morton, Registration; Richard C. Steele, Publicity; and Mrs. Robert B. Service, Ladies Committee.

War Department Citations for Carter, Stewart, and Troper

Their many friends throughout N. A. C. A. will be pleased to learn of the well-earned citations recently awarded Major General Arthur H. Carter, Colonel Andrew Stewart, and Colonel Morris C. Troper by the War Department. Major General Carter received the Oak Leaf Cluster to the Distinguished Service Medal for his outstanding work as Director of the Fiscal Division, Purchases and Contract Branch, Office of the Under Secretary of War and as Fiscal Director, Headquarters, Army Service Forces. Colonel Stewart was awarded the Legion of Merit for his distinguished service as

Chief, Accounting and Audit Supervisory Branch, Fiscal Division, Headquarters Services of Supply, and as Deputy Director, Office of Fiscal Director, Headquarters, Army Service Forces. Colonel Troper was awarded the Legion of Merit for outstanding service as Chief of the Cost Analysis Section, and later of the reports Section of the Fiscal Division, Headquarters, Services of Supply, and as Chief of the Coordination and Reports Branch, Office of the Fiscal Director, Headquarters, Army Service Forces.

New Fort Worth Chapter Chartered

At its meeting on October 26, the National Board granted a charter for a new chapter in Fort Worth, Texas. The new chapter, sponsored by the Dallas Chapter, begins operation with forty-seven charter members and brings the total of N. A. C. A. chapters to eighty-three. The following officers and directors have been elected:

President—F. Howard Zahn, American Cyanamid & Chemical Corp., Fort Worth, Texas.

Vice Presidents—Thomas N. Jenness, Jr., McCammon, Morris, Pickens & Mayhew, Fort Worth, Texas; Frank M. Benton, J. Warren Day & Co., Fort Worth, Texas.

Secretary—George E. Hart, Comptometer Co., Fort Worth, Texas.

Treasurer—Leo W. O'Dell, Emperor Oil Co., Fort Worth, Texas.

Directors—Joseph S. Judd, Southwestern Greyhound Lines, Inc., Fort Worth, Texas. George E. Luck, International Business Machines Corp., Fort Worth, Texas, Wayne E. Cochrum, Helm Manufacturing Co., Fort Worth, Texas. Carl Dannenfelser, Consolidated Vultee Aircraft Corp., Fort Worth, Texas. George H. Harwell, Elliott & Waldron Abstract Companies, Fort Worth, Texas. Homer L. Davis, Fort Worth Div. of Distribution, Lone Star Gas Co., Fort Worth, Texas. Paul H. Laverty, Certified Public Accountant, Fort Worth, Texas.

Correction in Chapter Officers List

In the "List of National and Chapter Officers and Directors" issued to chapter officers and directors earlier in the chapter year, the list of directors of the New York Chapter was incomplete. The two following directors should be added to that list:

Education—Thurber H. Bierce, Peat, Marwick, Mitchell & Co., 70 Pine St., New York 5, N. Y.

Special Activities—Frederick L. Burns, Seaboard Commercial Corp., 1819 Broadway, New York, N. Y.

CHAPTER MEETINGS

December, 1945

Chapter *Meeting Place*	*Date*	*Subject and Speaker*
Akron Portage Hotel	18	*Cost Allocations and Commodity Pricing* William A. Bechler, Assistant Comptroller, The B. F. Goodrich Co.
Albany O'Connor's Restaurant	18	*Internal Audit* F. L. Palmer, Auditor, F. C. Huyck & Sons.
Atlanta Atlanta Biltmore Hotel	18	*Recent Changes in Income and Excess Profits Taxes Affecting Corporations* A. M. Hoffar, Manager, Tax Department, Arthur Andersen & Co.
Baltimore Emerson Hotel	18	*The Job Ahead for the Industrial Accountant* Wyman P. Fiske, Secretary, National Association of Cost Accountants.
Binghamton Hotel Arlington	13	*The Future of Banking* Thomas A. Wilson, President, Marine Midland Trust Co.
Birmingham Hotel Thomas Jefferson	19	*Budgets and Forecasts* J. G. Bradbury, Vice President, Southern Bell Telephone & Telegraph Co.
Boston Copley Plaza Hotel	18	*Federal Taxation* Randolph E. Paul, Partner, Lord, Day & Lord.
Bridgeport Stratfield Hotel	20	*Importance of Property Investment Control* A. B. Hossack, Executive Vice President, American Appraisal Co., Inc.
Brooklyn Central Branch, Y. M. C. A.	12	*Recent Developments in Federal Taxation* Virgil P. Ettinger, Tax Consultant, New York.
Buffalo Church of the Covenant	20	*Looking Through the Telescope* Arthur C. Horrocks, Public Relations Director, Goodyear Tire & Rubber Co., Inc.
Calumet Hotel Gray	18	*Psychology in Office Management* Fred A. Replogle, Partner, Rohrer, Hibler & Replogle
Cedar Rapids Hotel Roosevelt	19	*Case Studies in Deflation Planning* Seth L. Winslow, Partner, McKinsey, Kearney & Co.
Chattahoochee Valley	10	*Current Problems in Federal Taxation—The New Revenue Act* Del R. Paige, Resident Partner, Ernst & Ernst.
Chattanooga Hotel Patten	20	*Reports to Management for Control Purposes* Keith J. Harris, Secretary and Treasurer, Ross-Meehan Foundries.
Chicago The Furniture Club of America	20	*Information Please*

Chapter Meeting Place	*Date*	*Subject and Speaker*
Cincinnati Hotel Gibson	20	*1945 Federal Income Taxes* Frank C. Callahan, Partner, Richard Smethurst & Co.
	6	*The Budget Analyst and Cost Accountant* S. M. Bender, Cost Auditor, Libbey Glass Div., Owens-Illinois Glass Co.
Cleveland The Carter Hotel	20	*Accounting and Tax Problems Relating to War Facilities* William Y. Armstrong, District Manager, American Appraisal Co.
Columbus Ft. Hayes Hotel	10	*Current Problems in Federal Taxation of Corporate Income* Joseph A. Maloney, Certified Public Accountant and Tax Attorney.
Cuba Habana Yacht Club	26	*World Organization for Peace* Dr. Cesar Salaya de la Fuente, Director of School of Diplomatic and Consular Law, Faculty of Social Sciences and Public Law, University of Havana, and President, Inter-American Institute of Public Law and Social Sciences.
Dallas Melrose Hotel	21	*Payroll Procedures (A Case Study) and Related Problems* W. M. Merritt, Assistant Comptroller, Todd Houston Shipbuilding Corp.
Dayton Van Cleve Hotel	11	*Limitations of Cost Accounting* William A. Paton, Professor of Economics and Accounting, University of Michigan.
Decatur Leland Hotel	29	*Payroll Accounting in the Postwar Period* L. E. Zastrow, Assistant Controller, Bucyrus-Erie Co.
Denver Cosmopolitan Hotel	11	*Current Federal and State Income Tax Developments and Changes in the Tax Laws* Chairman: A. B. Fielding, Haskins & Sells.
Des Moines Commodore Hotel	20	*Case Studies in Deflation Planning* Seth L. Winslow, McKinsey, Kearney & Co.
Detroit Detroit-Leland Hotel	20	*Present Position of the United States in World Finance and Trade* Leonard Watkins, Professor of Economics, University of Michigan.
Erie Moose Club	17	Panel Discussion: *Merit Rating in Pennsylvania* Discussion Leader: Quentin C. Horsman, Treasurer, Bliley Electric Co.
Evansville McCurdy Hotel	20	*Machine Accounting Methods* A. B. Connally, Friden Calculator Sales Agency; M. F. Hundley, Monroe Calculating Machine Co.; and J. F. Kuhn, Burroughs Adding Machine Co.
Fort Wayne Chamber of Commerce	18	*Reconversion of Cost Accounting Procedures* H. G. Barden, Ernst & Ernst.

Chapter / Meeting Place	Date	Subject and Speaker
Grand Rapids Rowe Hotel	18	Panel Discussion: *The 1945 Tax Law* D. G. Knapp, Assistant Treasurer and Controller, C. M. Benson, Chief Accountant, and R. L. Warner, Member of Tax Dept., The Upjohn Co.
Greenwich Hugo's Piccadilly Restaurant	18	*The Accountant's Viewpoint on the Cost to Sell* N. R. Caine, N. R. Caine & Co.
Hagerstown Hotel Alexander	20	*Accounting and Price Control During Reconversion* Walker E. Campbell, Director, Consumer Products Accounting Div., Office of Price Administration.
	6	Panel Discussion: *Personal Income Taxes*
Hampton Roads Albany Restaurant, Norfolk	21	*Ship Construction and Repair Costs* Robert I. Fletcher, Controller, Newport News Shipbuilding & Drydock Co.
Harrisburg Penn-Harris Hotel	11	*Accounting Aspects in Connection with Federal Bureau of Investigation Work* James W. Going, Special Agent, Federal Bureau of Investigation.
Hartford Farmington Country Club, Farmington	11	*Tax Trends* Edward H. Bengtson, Scovill Manufacturing Co.
Houston Y. M. C. A.	19	*Relation of Costs to Foreign Trade Improvement* St. John Garwood, Attorney-at-Law.
Indianapolis Lincoln Hotel	19	Panel: *"Information Please" on Costs, Auditing, General Accounting, and Taxation* Chairman: J. B. Baerncopf, Geo. S. Olive & Co.
Jackson Heidelberg Hotel	20	*Federal Income Tax* Dick D. Quin, Certified Public Accountant, Jackson.
Jamestown Hotel Jamestown	18	*The Cost Accountant as Management's Master Key to the Factory* Robert P. Schermerhorn, Certified Public Accountant, Buffalo.
Kansas City	17	*Corporate Income and Excess Profits Taxes* Perry Shrader, Attorney, Kansas City.
Lancaster Hotel Sutter	14	*Financing the Peace* H. C. Culshaw, Vice President, The Pennsylvania Co.
Lehigh Valley Hotel Traylor, Allentown	14	*Pennsylvania Taxes* Harry Margolis, Harry Margolis & Co.
Los Angeles Scully's Cafe	11	*Control of Overhead Costs—The Dangers Inherent in the Conversion Period* P. L. Fredericks, Assistant to Director Management Control, North American Aviation, Inc.

Chapter *Meeting Place*	*Date*	*Subject and Speaker*
Louisville Brown Hotel	18	*Cost to Industry of Proposed State Legislative Program* Louis J. Bosse, Managing Director, Associated Industries of Kentucky.
Maine (State of) Lafayette Hotel, Portland	21	*The Place of Cost Accounting in the Postwar Competitive Market* Clinton W. Bennett, Partner, Cooley & Marvin.
Memphis Hotel Gayoso	19	*Federal Taxation* E. C. Boye, Resident Partner, Peat, Marwick, Mitchell & Co.
Milwaukee Milwaukee Athletic Club	17	*Control Accounting for Material Costs* R. C. Roll, Bendix Aviation Corp.
Minneapolis Curtis Hotel	10	Panel Discussion: *Effective Accounting Reports* Chairman: Arthur H. Smith, Vice President and Comptroller, General Mills, Inc.
Muskegon Occidental Hotel	17	*Budgetary Control* Gilbert A. Peters, Treasurer, Kaydon Engineering Corp.
Nashville Andrew Jackson Hotel	11	*Postwar Valuation of Plant* E. D. Burk, President, Coats & Blanchard Co.
Newark Hotel Robert Treat	13	*The Tax Law—Recent Changes, Developments, and Trends* Alger B. Chapman, Commissioner of Taxation and Finance of the State of New York, and President of the State Tax Commission.
New Hampshire The Carpenter Hotel, Manchester	18	*Taxes* John L. Carey, Secretary, American Institute of Accountants.
New Haven Hotel Duncan	18	*Reconversion and Industrial Accounting* William F. Burke, Assistant Controller, Scovill Manufacturing Co.
New Orleans Jung Hotel	12	*Federal Taxation in War and Peace* Roy Blough, Assistant to the Secretary, U. S. Treasury Department.
New York Hotel New Yorker	17	*Peacetime Problems of the Financial Executive* Henry C. Perry, Treasurer, Heywood-Wakefield Corp.
Peoria Jefferson Hotel	19	*Payroll Accounting in the New Era* Leonard E. Zastrow, Assistant Comptroller, Bucyrus-Erie Co.
Philadelphia Kugler's Chestnut St. Restaurant	13	Debate: *Standard Costs Versus Actual Costs* Chairman: Edwin W. Hart, Certified Public Accountant, Philadelphia.
Pittsburgh Fort Pitt Hotel	19	*Using Costs to Control Business Activity* Eric A. Camman, Partner, Peat, Marwick, Mitchell & Co.

Chapter Meeting Place	Date	Subject and Speaker
Portland Heathman Hotel	18	*Job Evaluation and Wage Incentives* Donald E. Ackerman, Management Consultant, McKinsey & Co.
Providence Narragansett Hotel	13	*The Value of Cost Data to the Manufacturer* Ira Mosher, President, National Association of Manufacturers.
Reading Wyomissing Club	14	*Public Utility Accounting* Edgar O. Dreas, Controller, Metropolitan Edison Co.
Richmond Hotel John Marshall	14	*Engineering Aspects of the Development of Standard Costs* W. F. Bennett, Supervisory Cost Engineer, Ernst & Ernst.
Rochester Hotel Seneca	19	*Wages and Salary Administration and Their Effects on Costs* R. D. Kinsella, Assistant Superintendent in charge of Wage Standards, Eastman Kodak Co.
Rockford Hotel Faust	13	*The Future of Wage Stabilization* Gordon W. Hostetter, Manager, Toledo Branch, National Metal Trades Association.
Saginaw Valley Hotel Bancroft	12	*Cost Reduction Through Time and Motion Study* Henry J. Christ, Jr., Supervisor of Time and Motion Study, Saginaw Steering Gear Div., General Motors Corp.
St. Louis Coronado Hotel	11	*Current Corporate Tax Problems* James O. Mahon, Jr., Lybrand, Ross Bros. & Montgomery.
San Francisco Engineer's Club	19	*Costs* Adrian Metzger, Auditor, Schmidt Lithograph Co.
Scranton Hotel Casey	17	*Job Evaluation, Salary Ranges, Merit Rating Incentives and Their Relation to the Accounting Department* Nicholas L. A. Martucci, Chief Job Analyst, National Union Radio Corp.
South Bend LaSalle Hotel	11	*Practical Views on Taxation* A. B. Clohosey, Director, Washington Office, Research Institute of America.
Springfield Sheraton Hotel	19	*Current Tax Problems* D. B. Chase, Lecturer, New York University.
Syracuse Hotel Syracuse	13	Panel Discussion: *Payroll Accounting Systems and Methods* Panel Members: Robert Jones, Assistant to Treasurer, Crouse-Hinds Co.; A. H. Pellenz, General Factory Accountant, L. C. Smith & Corona Typewriters, Inc.; S. M. Anderson, Jr., Chief Accountant, Lennox Furnace Co., Inc.; and K. I. DuPre, Assistant Controller, Rollway Bearing Co., Inc.

Chapter *Meeting Place*	*Date*	*Subject and Speaker*
Toledo Secor Hotel	18	*Costs and the Labor Viewpoint* Edward T. Cheyfitz, National Chairman, Casting Div., Mine, Mill & Smelter Workers.
Tri-Cities Hotel Blackhawk, Davenport	18	*Case Studies in Deflation Planning* Seth L. Winslow, Partner, McKinsey, Kearny & Co.
Tulsa Mayo Hotel	19	*The Accountant's Roll in Loss Adjustments Under Use and Occupancy Insurance* J. P. Compton, Assistant Secretary-Treasurer, American Asphalt Roof Corp.
Utica Hotel Hamilton	10	*Corporate Financial Planning During the Transition Period* Theodore Lang, Professor of Accounting, New York University.
Wabash Valley Terre Haute House, Terre Haute	11	*Wage Incentive Techniques and Personnel Problems Incident Thereto* B. M. Sayre, Benedict M. Sayre & Co.
Washington Hotel 2400	19	*Job Ahead for Industrial Accountants* Wyman P. Fiske, Secretary, National Association of Cost Accountants.
Wichita Broadview Hotel	18	*Tax Panel* Chairman: C. W. Rossdutcher, Fox, Morgan & Rossdutcher.
Williamsport Lycoming Hotel	10	*Material and Production Control* M. E. Mengel, Burroughs Adding Machine Co.
Worcester Sheraton Hotel	20	*Federal Taxation* Roy Blough, Assistant to the Secretary, Treasury Department.
York Hotel Yorktowne	19	*Individual Income Taxes* Ezra Miller, Kochenour & Rissinger.
Youngstown Tippecanoe Country Club	19	*Control of Inventories* W. K. Bonte, General Accounting Dept., Republic Steel Corp.